

Message Text

SECRET

PAGE 01 JIDDA 05164 01 OF 02 131215Z
ACTION NEA-10

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FM AMEMBASSY JIDDA
TO SECSTATE WASHDC PRIORITY 2690
INFO USMTM DHAHRAN

S E C R E T SECTION 1 OF 2 JIDDA 5164

E.O. 11652: GDS
TAGS: MARR, MASS, BENC, BTIO, SA
SUBJ: LITTON INDUSTRIES' AIR COMMAND SYSTEM, A \$2 BILLION
CONTRACT PROPOSAL HITS PRICE SNAG

REF: (A) JIDDA 2394, (B) USMTM DHAHRAN 061345Z

1. BACKGROUND SUMMARY: LITTON INDUSTRIES REPRESENTATIVES IN SAUDI ARABIA HAD INFORMED THE EMBASSY IN MARCH THAT THEY ANTICIPATED FAVORABLE ACCEPTANCE OF THE \$2 BILLION CONTRACT FOR THE SAUDI AIR DEFENSE COMMAND AND CONTROL SYSTEM. THE PRINCIPAL COMPANY REPRESENTATIVE, LAWRENCE MANN, HAD REITERATED THE COMPANY'S CONFIDENCE IN JUNE 1978. DURING THE AMBASSADOR'S CONVERSATION WITH PRINCE SULTAN, MINISTER OF DEFENSE AND AVIATION, ON JULY 2, 1978, THE LATTER EXHIBITED CONSIDERABLE OPPOSITION TO THE HIGH COST OF THE PROPOSAL PRESENTED TO HIM - \$2.4 BILLION - AND THE ALLEGED "TAKE IT OR LEAVE IT" ATTITUDE OF LITTON. HE CLAIMED THAT THERE WERE OTHER COMPANIES AND ALTERNATIVES. HE SUGGESTED WE ADVISE LITTON TO REDUCE THE PRICE. HE WAS CONSIDERING THE FMS ROUTE. THE EMBASSY DISCUSSED THE PROBLEM AT LENGTH WITH LITTON OFFICIALS IN COUNTRY ON JULY 10 WHO AGREED THAT DEPARTMENT AND DOD SHOULD BE INFORMED AND ADVISE TOP
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PAGE 02 JIDDA 05164 01 OF 02 131215Z

MANAGEMENT OF LITTON IN PARALLEL WITH THEIR INTENDED REPORT. EMBASSY MADE SUGGESTIONS FOR COMPANY ACTIONS THAT WERE ACCEPTED BY LITTON OFFICIALS. END SUMMARY.

2. WITH SOME CONFIDENT ELATION, LITTON INDUSTRIES REPS INFORMED THE EMBASSY THAT FINAL TOUCHES WERE BEING PUT TO A PROPOSAL TO SAG FOR ESTABLISHMENT OF AN AIR DEFENSE

CONTROL SYSTEM FOR THE KINGDOM (REFTEL A). THE COMPANY'S CONFIDENCE REACHED THE LEVEL OF PLANNING FOR THE ASSIGNMENT, HOUSING AND SUPPORT SERVICES FOR 450 FAMILIES IN SAUDI ARABIA. MR LARRY MANN, LITTON'S MAJOR IN-COUNTRY REPRESENTATIVE, CALLED ON THE AMBASSADOR IN JUNE TO GIVE A STATUS REPORT ON THE PROPOSAL AND INDICATED THAT ALL WAS GOING WELL, AND THAT THE PRICE FORMULATION WOULD BE PRESENTED IN JULY 1. WHEN ASKED BY THE AMBASSADOR IF THERE WAS ANYTHING THE EMBASSY COULD DO TO HELP, MANN REPLIED THAT EVERYTHING SEEMED WELL IN HAND.

3. ON JULY 2, THE AMBASSADOR MET WITH PRINCE SULTAN, WHO ASKED FOR THE PRESENCE OF BG CARL CATHEY, USMTM, SAUDI ARABIA. PRINCE SULTAN PROCEEDED TO EXPRESS STRENUOUS OBJECTIONS TO THE HIGH PRICE TAG, APPROXIMATELY \$2.4 BILLION, PRESENTED BY LITTON WHICH HE DESCRIBED AS GREEDY. SULTAN TOOK SPECIFIC EXCEPTION TO THE ALMOST \$300 MILLION TABBED FOR RESEARCH AND DEVELOPMENT WHICH HE FIGURED IS A PAYMENT FOR FUTURE DEVELOPMENTS WHICH WILL BE AVAILABLE TO OTHER COUNTRIES. HE ALSO OBJECTED STRENUOUSLY TO THE \$72 MILLION COST ADDITION BASED ON NON-ACCEPTANCE FROM SAG BY THE END OF JULY. OTHER PROPOSAL POINTS OBJECTED TO WERE THE \$35 MILLION PLANNING COSTS FOR 6 HOUSING LOCATIONS, PAYMENT OF ABOUT \$1.2 BILLION IN THE FIRST YEAR BEFORE LITTON DELIVERS ANYTHING, AND ALLEGEDLY EXCESSIVE MAN-MONTH COSTS. MORE COMPLETE DETAILS ARE REPORTED IN SECRET

SECRET

PAGE 03 JIDDA 05164 01 OF 02 131215Z

REFTEL B. PRINCE SULTAN ALSO OBSERVED THAT WHEREAS SAUDI LAW FORBIDS AGENTS, LITTON IS IN A JOINT VENTURE WITH A SAUDI FIRM. THE SAUDI FIRM IS XENEL INDUSTRIES, AN ALI REZA AFFILIATE. THE LAST SIGNIFICANT OBJECTION MADE BY PRINCE SULTAN WAS THAT THE MAN-MONTH ESTIMATE OF \$16,000 COMPARED UNFAVORABLY WITH THE \$6.7,000 IN OTHER MODA CONTRACTS.

4. IN ADDITION TO THE ABOVE OBJECTIONS, PRINCE SULTAN FUMED THAT LITTON HAS REFUSED TO NEGOTIATE. HE INFERRED THAT THE COMPANY HAS MADE THE OFFER ON A "TAKE IT OR LEAVE IT" BASIS, GIVING HIM THE IMPRESSION THAT HE HAS NO OTHER CHOICE. IF THIS WAS THE COMPANY'S ATTITUDE SULTAN SAID, THE SAG WOULD BE PREPARED TO LEAVE IT AND GO TO ANOTHER COMPANY, POSSIBLY SWISS OR "ANOTHER NATIONALITY". THE AMBASSADOR RESPONDED WITH REGRETS ABOUT THIS DEVELOPMENT BUT POINTED OUT THAT THERE MAY BE LITTLE HE CAN DO BECAUSE IT IS A PRIVATE CONTRACT. PRINCE SULTAN STATED HE INTENDED TO ASK GENERAL CATHEY TO CONFER WITH COLONEL MALIK OF HIS OFFICE REGARDING WHETHER THE SAG SHOULD GO TO THE FMS ROUTE FOR THE PROJECT. THE AMBASSADOR THEN POINTED OUT THE POTENTIAL DELAY FOR THE PROJECT IF FMS BECAME A

CHOICE NOW. PRINCE SULTAN AGREED BUT ASKED THE AMBASSADOR TO CONTACT THE LITTION COMPANY AND REINFORCE HIS VIEWS. THE AMBASSADOR AGREED TO THIS AND SAID HE WOULD HELP IN ANY WAY POSSIBLE.

5. ON JULY 9, THE EMBASSY'S POLITICAL AND ECONOMIC COUNSELORS DISCUSSED THE PROBLEM WITH T.M. MCDONALD, VICE PRESIDENT FOR BUSINESS AND DEVELOPMENT, ND TOM WHITE, COMPTROLLER OF LITTION INDUSTRIES, SINCE LARRY MANN, THE RIYADH-BASED REPRESENTATIVE, HAD DEPARTED FOR THE U.S. PRESENTED WITH A REVIEW OF PRINCE SULTAN'S OBJECTIONS AND THE POTENTIAL JEOPARDY TO THE CONTRACT, MR MCDONALD STATED THAT THE \$2.4 BILLION COST HAD BEEN SHAVED ABOUT \$185 MILLION. THE CUTS HAD BEEN MADE IN THE ESTIMATES
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SECRET

PAGE 04 JIDDA 05164 01 OF 02 131215Z

CALCULATED ON THE PREMISE OF HIGHER TAX COSTS UNDER SECTION 911, THE COSTS PROJECTED FOR DECLINING VALUE OF THE DOLLAR, AND THE

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PAGE 01 JIDDA 05164 02 OF 02 131231Z
ACTION NEA-10

INFO OCT-01 ISO-00 PM-05 NSC-05 SP-02 SS-15 CIAE-00
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TO SECSTATE WASHDC PRIORITY 2691
INFO USMTM DHAHRAN

S E C R E T SECTION 2 OF 2 JIDDA 5164

SHIFT AT MIDPOINT ON THE \$72 MILLION PENALTY FOR NON-SIGNATURE BY JULY 31, 1978, AS WELL AS THE \$35 MILLION INCLUDED IN THE TAB, WHICH IS REALLY AN A&E COST ON MILITARY WORKS THAT WILL BE PAID TO A SUBCONTRACTOR. IN EFFECT, THE REAL REDUCTION AMOUNTS TO \$150 MILLION. REGARDING OTHER ALLEGED OVER-COSTS, MR MCDONALD STATED

THAT THE PROBLEM CONCERNING RESEARCH AND DEVELOPMENT IS DUE TO AN UNFORTUNATE CHOICE OF WORDS. THE COSTS REALLY REPRESENT TAILORING THE SYSTEM'S TECHNOLOGY TO FIT SAUDI ARABIA'S CLIMATIC, GEOLOGICAL, AND OTHER SPECIAL NEEDS. REGARDING HOUSING AND OTHER COSTS, MCDONALD AND WHITE STATED THAT THESE HAD TO BE BUILT-IN BECAUSE THE PROJECT WOULD LAST FOR SIX YEARS. TO COVER POTENTIAL INFLATION, THE COMPANY'S DATA WAS BASED ON A WORST CASE SITUATION. MCDONALD ALSO STATED THAT, DURING HIS NEGOTIATIONS ON THE PROJECT FOR OVER 9 MONTHS WITH COLONEL MALIK, HE HAD PROPOSED A COST-PLUS OR A COST ADJUSTMENT CLAUSE BASED ON INFLATION OR DEFLATION RATES, BUT THAT MALIK WOULD NOT EVEN CONSIDER IT. THIS WAS STILL THE SAG POSITION BUT LITTON REPS STATED THAT THE COMPANY WOULD IMMEDIATELY ACCEPT COST-PLUS TERMS.

6. E/C COUNSELOR ADVISED LITTON REPS THAT, TO COUNTER-
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PAGE 02 JIDDA 05164 02 OF 02 131231Z

ACT PRINCE SULTAN'S FEELINGS, THE COMPANY WAS COMMITTED TO A TAKE IT OR LEAVE IT ATTITUDE, IT MIGHT BE USEFUL IF THE PRESIDENT OF LITTON WOULD FLY TO RIYADH OR TAIF, IF SULTAN WAS THERE, IN THE COMPANY'S AIRCRAFT TO DISCUSS THE MATTER WITH THE PRINCE PERSONALLY. THIS WOULD INDICATE LITTON'S CONCERN AND MIGHT ASSUAGE SULTAN'S RUFFLED FEELINGS. WHEN THIS MEETING OCCURRED, THE CONTRACT SOTS COULD BE REVIEWED IN DETAIL. MCDONALD AND WHITE RESPONDED POSITIVELY TO THIS SUGGESTION. THE FORMER STATED THAT IT WOULD BE USEFUL IF THE DEPARTMENT OF STATE WOULD RECOMMEND THIS TO THE PRESIDENT OF LITTON, FRED W. O'GREEM. EMBASSY OFFICERS AGREED TO TRANSMIT THIS SUGGESTION TO THE DEPARTMEMTN.

7. WE ASKED LITTON REPS WHETHER THERE WAS ANY COMPETITION FOR THE CONTRACT. MR MCDONALD STATED THAT HE UNDERSTOOD THOMPSON CSF OF FRANCE WAS ANGLING FOR THE PROJECT THROUGH AKRAM OJEH. WE OBSERVED THAT THERE HAD BEEN SOME ADVERSE PUBLICITY RECENTLY REGARDING OJEH WHICH APPEARED TO HAVE SAG BLESSING, SINCE IT WAS AN OPEN LETTER BY THE MINISTER OF INDUSTRY, GHAZI GOSAIBI, PUBLISHED IN THE LOCAL PRESS.

FHI: WE UNDERSTAND FROM LOCAL SOURCES THAT PRINCE SULTAN HAS BEEN AKRAM OJEH'S SECRET SPONSOR IN THE KINGDOM. IF SO, THERE MAY BE MORE FIRE THAN SMOKE BEHND SULTAN'S PROTESTATIONS. IN ADDITION, THE ANTICIPATED WINNING OF A LARGE PROJECT BY FRENCH INTERESTS AFTER KING KHALID'S MAY 1978 VISIT TO FRANCE, HAS NOT YET OCCURRED. THE FRENCH MAY BE PUSHING FOR THIS ONE.

8. ON JULY 10, THE AMBASSADOR CONTACTED PRINCE SULTAN

AND REPORTED THAT HE HAD TALKED TO LITTON. HE COULD
ASSURE PRINCE THAT LITTON WAS WILLING TO NEGOTIATE AND
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PAGE 03 JIDDA 05164 02 OF 02 131231Z

HAD ALREADY AGREED TO REDUCE COST. PRINCE SULTAN SAID
THAT LITTON HAD CUT \$150 MILLION BUT THAT HE EXPECTED
\$500 MILLION TO BE SLICED FROM THE ORIGINAL PROJECT COST
ESTIMATES. HIS USE OF THE \$150 MILLION FIGURE INDICATED
HIS DEPTH OF KNOWLEDGE OF THE PRICES AND TERMS AND THAT
HE HAD ALSO RECOGNIZED THE \$35 MILLION A&E COST AS SUP-
PLEMENTAL TO THE PROJECT. HE WAS DELIGHTED TO KNOW OF
THE PROSPECT THAT THE PRESIDENT OF LITTON WOULD COME TO
SAUDI ARABIA TO SEE HIM PERSONALLY AND WELCOMED THE VISIT.

9. AT ITS DISCRETION, WE RECOMMEND THAT THE DEPARTMENT
APPROACH THE PRESIDENT OF LITTON TO INFORM HIM ABOUT THE
COMPANY'S PROBLEMS AND URGE HIM TO MAKE THE TRIP TO SAUDI
ARABIA. THE DEPARTMENT'S ADVICE IN HANDLING THIS IMPOR-
TANT PROJECT WILL BE APPRECIATED AS WELL AS ANY INFORM-
TION ON REACTION TO THE PROBLEMS BY THE TOP ECHELON OF
THE COMPANY. CONSIDERING THE SCOPE AND VALUE OF THE
PROJECT, THE EXPORT MULTIPLIER EFFECTS, AND OUR BALANCE
OR PAYMENTS, WE SUGGEST THAT THIS BE HANDLED AT APPROP-
RIATE LEVELS IN THE DEPARTMENT.

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